telecommunications market including interstate services originating or terminating in Connecticut and will focus on the ability of competitors to offer packages of products and services. Because the market will consist primarily of bundles of telecommunications services, including local exchange service, the "relevant market" for determining SAI's market power following the proposed reorganization, should be the market of bundled telecommunications products. However, the Company states that even if the relevant market were deemed by the Department to be the Connecticut retail local exchange market, SAI will not have unfair market power because, as a result of Public Act 94-83 and the 1996 Federal Act, that market is now fully "contestable."

The Company further argues that while SAI will initially have a high share of the local exchange market, market share alone does not necessarily determine market power (i.e., the ability to control prices). The Company contends that the Public Act and the 1996 Federal Act have created a framework in which the Telco must resell all of its services and unbundle all of its network for market participants. Prices for Telco services must be available to all CLECs on the same terms and conditions. Moreover, SAI will be subject to all antitrust laws. Additionally, given the number of certified CLECs in the local exchange market, SAI will not be able to raise its prices without fear that other CLECs purchasing the same services from the Telco will undercut SAI's price. Therefore, SAI will not have market power to control prices following the reorganization.

The Company argues that reliance upon market share statistics in this instance is likely to be an inaccurate or misleading indicator of market power. The Company claims entry by prospective competitors into the Connecticut local exchange market is extremely easy. The Company further states that due to the 1996 Federal Act, all CLECs, including SAI, can purchase all Telco services for resale in the retail market. The Company contends that previous barriers to market entry, such as the prohibitive cost of constructing a network and facilities are no longer present. In the Company's view, CLECs can now compete in the local exchange market without a significant investment in either technology or personnel and it is for these reasons that the Company believes SAI's market share will not be sustainable over time.

Finally, the Company contends SAI's lack of market power will be further supported by the Telco's imminent loss of local exchange market share. The Company states that, while the Telco's customers will move to SAI on the effective date of the reorganization, the Telco expects significant market activity prior to that date. The Company expects a reduction in the Telco's market share for residential and business local service customers by January 1, 1998. The Company notes that the Telco has begun to experience local residential and business market share loss across the state, and expects by year end to lose even greater market share. Company Brief, pp. 34-49; Company Reply Brief, pp. 28-32.

4. Customer Marketing

The Company contends that some form of neutral customer education will afford customers opportunity to be better informed of their local carrier choices prior to the reorganization. While the Telco initially proposed bill inserts and public service announcements, the Company opposes any formal balloting process because of the inherent complexity and the potential for customer confusion. The Company further argues that balloting would be costly and is not necessary to make the local exchange market competitive. In support of its argument against balloting, the Company notes that when intrastate equal access was implemented, the Department found that customer balloting was not necessary. The Company points out that the market is now fully competitive, five months after the implementation of equal access. In the Company's view, there is no reason to believe that the local exchange market would respond differently. In lieu of balloting, therefore, the Company suggests that a combination of a neutral education program and CLECs' own marketing efforts will be sufficient to ensure that customers know they have choices. The Company also supports a customer information center that would serve as a neutral point of contact for customers as well as objective letters sent to all customers by a third party to inform customers of their choices. Company Brief, pp. 49-51.

5. Cost Accounting Manual

The Company argues that the Telco's Cost Allocation Manual (CAM) and the current regulatory environment provide sufficient protection against cross-subsidization even upon reorganization. The Company states that following the reorganization, the Telco will continue to be subject to §§251 and 252 of the 1996 Federal Act, applicable antitrust laws prohibiting predatory pricing and other anti-competitive conduct, the accounting rules set forth in 47 C.F.R. Parts 32 and 64 and the CAM. The Company claims that this body of regulation provides detailed requirements regarding the allocation of costs between regulated and non regulated affiliates. The Company asserts that these safeguards are appropriate to ensure that the Telco is not permitted to improperly shift costs among itself, SAI and its other unregulated affiliates.

The Company also asserts that any redesignation on the corporate books of retail assets to SAI from the Telco should be accounted for at net book value. The Company argues that the proposed reorganization is not a "transaction" within the meaning of the CAM, but is a corporate reorganization caused by major industry and regulatory changes. Consequently, the Telco's CAM is not applicable in this situation because the affiliate transaction rules do not apply. According to the Company, those rules were designed to apply only to routine and ongoing transfers of goods and services that might result in systematic cross-subsidization of a non-regulated affiliate by the regulated entity.

Lastly, the Company contends that given the increasingly competitive nature of the telecommunications market in Connecticut and the proposed corporate reorganization, Holding Company and Telco restrictions and reporting requirements imposed by the Department over the past several years are no longer necessary. The Company argues that subsequent to the corporate reorganization, these restrictions and reporting requirements should be eliminated. Company Brief, pp. 51-55.

B. OFFICE OF CONSUMER COUNSEL (OCC)

1. Reorganization Proposal

OCC states that the Company's proposal is truly a creative approach to overturning certain requirements in state and federal law and ignores existing channels through which SNET should seek relief from problems it has discussed in this proceeding. OCC cites as an example the 1996 Federal Act's inclusion of the "two percent rule" to provide suspensions or modifications of requirements imposed on local exchange carriers of SNET's size. 47 U.S.C. § 251(f)(2). OCC also notes that Connecticut law permits telephone companies to follow certain procedures to reclassify a service to a less regulated designation if market conditions for that service merit such a reclassification.

OCC contends that SNET's assertion that its proposal will benefit competition does not stand up in the context of the Connecticut and federal laws. OCC states that recent federal and state policy developments make the transition from monopoly telecommunications markets to competitive markets by weakening the market power of the monopoly service provider and not shifting that power to different parts of its corporate structure. OCC claims that a primary purpose of both the 1996 Federal Act and Public Act 94-83 is to relieve the Company of its monopoly, requiring it to lose a portion of its market share and related revenues. OCC asserts that it has no interest in imposing any regulatory restrictions on the Company for its own sake; rather, its interest is in ensuring that federal and state law is adhered to and that competition thrives in Connecticut for the benefit of telecommunications consumers. According to OCC, until effective local service competition emerges in Connecticut, particularly for residential consumers, the consumer's interest will only be protected by continuing Departmental regulation of SNET. OCC contends that the Company's proposal would defeat that interest. Accordingly, as a matter of both state and federal law as well as sound public policy, OCC recommends the Department reject SNET's reorganization proposal. OCC Brief, pp. 5-7; OCC Reply Brief, pp. 5.

2. Successor of an ILEC

Noting the Company's proposal to transfer its retail operations to SAI and no longer offer retail local exchange service from the Telco, OCC maintains that Congress foresaw and prohibited this sort of corporate shuffle to avoid the central requirements of the 1996 Federal Act when it included in the definition of ILEC any "successor or assign" of an ILEC. OCC contends that the monopoly power which Congress was trying to break is not innate to the particular corporate entity of the original ILEC but rather it resides in the services, functions, and facilities of the ILEC, all of which can be transferred to another corporate entity through succession or assignment. According to OCC, as a "successor or assign" of the Telco, SAI is itself an ILEC with respect to its retail service. OCC concludes that treating SAI as a CLEC without the ILEC obligations would thus be a violation of the 1996 Federal Act.

OCC further contends that by imposing greater restrictions on ILECs than CLECs in the 1996 Federal Act, Congress created a disparate regulatory treatment for carriers providing similar services. OCC states that it is clear that Congress wanted ILECs to be forced to give up some of their monopoly power. In OCC's view, any attempt by the Company to subvert that intention is not legally defensible.

OCC is not persuaded by the Company's argument that SAI would be a CLEC, freed from the additional regulatory obligations imposed on ILECs under the 1996 Federal Act. OCC maintains that as a successor of the Telco SAI would be included in the definition of an ILEC and that the Company misinterprets the plain meaning of the terms "successor" and "assign" as well as FCC guidance on this issue. According to OCC, there is no question that these definitions describe the role that SAI is playing for the Telco under the Company's proposal. OCC contends that SAI is following the Telco into possession by inheritance or succession and that those inherited possessions include, among other things, the Telco's customer base, equipment, employees, reputation as a local telephone company and the strength of its brand.

OCC states that in evaluating the legality of the Company's proposal it is important to remember that the question before the Department is not whether the Telco may transfer its local exchange service to an affiliate. Rather, the issue is whether that affiliate may provide local exchange service and still be considered a CLEC while freeing the Telco from the resale pricing provision of §251(c)(4) of the 1996 Federal Act.

OCC also disagrees with SNET's contention that under the recent Non-Accounting Safeguards Order, SAI would not be treated as an assign of the Telco. According to OCC, the Non-Accounting Safeguards Order explicitly prohibits a BOC from transferring local exchange and exchange facilities and capabilities to "... another affiliate," in order to evade regulatory requirements. Non-Accounting Safeguards Order, ¶ 18. OCC states that the FCC disapproves of efforts by "one service provider to game regulatory requirements." Id. at ¶ 19. Additionally, OCC contends that the very fact that the 1996 Federal Act includes a services-based ILEC resale requirement alongside other, facilities-based requirements indicates Congress' recognition that wholesale access to an ILEC's services is essential to eliminating ILEC monopolies and to enabling new market entrants to compete. OCC claims that there is no indication that Congress saw the resale pricing requirement as somehow less important than the other provisions of §251(c) of the 1996 Federal Act. In OCC's view, it is hard to imagine that Congress intended to limit its definition of a "successor or assign" only to an entity that is the beneficiary of a transfer of facilities to the exclusion of services.

Further, OCC notes that in the Non-Accounting Safeguards Order, the BOCs, argued for a narrow definition of "successor or assign," proposing that an "affiliate could only be a successor or assign if it 'substantially take[s] the place of the BOC in the operation of one of the BOC's core businesses." Non-Accounting Safeguards Order at ¶ 303. Although the Department is not required to define the outer limits of the successor definition in this docket, OCC recommends that the Department adopt a definition at least as broad as the "core business" definition which the BOCs proposed in that FCC proceeding, and determine that the Company's retail local exchange business is a core business.

OCC maintains that a literal reading of §251(h)(1) of the 1996 Federal Act punctuation and clause designations requires that SAI be considered an ILEC if it had been offering local exchange service on the date of the 1996 Federal Act's enactment. However, OCC explains that such a literal reading of that subsection would do damage to the intent of the 1996 Federal Act and would render other provisions meaningless. OCC suggests that the Department include as part of its definition of an ILEC, a "successor or assign" of a carrier that meets both subparagraph (A) and clause (B)(i) of §251(h)(1) of the 1996 Federal Act.

Further, OCC contends that a literal reading of that section of the 1996 Federal Act would permit the Telco to transfer all of its assets, including its network to SAI, while essentially freeing SAI from the ILEC obligations imposed upon the Telco by the 1996 Federal Act. OCC argues that there would be no real difference between the Telco and SAI after the transfer except for a different name. According to OCC, given the ease with which ILECs could evade the explicit provisions of §251(c) of the 1996 Federal Act, (i.e., requirements that ILECs negotiate, interconnect, provide unbundled access, resell retail services at wholesale prices, provide notice of changes, and provide collocation) such requirements would become meaningless.

Additionally, OCC argues that a literal reading of §251(h)(1) of the 1996 Federal Act would run counter to Congress' intent in passing the legislation. OCC states that Congress intended to break the monopoly power of the ILECs by imposing additional obligations on them and not preserving the old monopolies in different corporate shells under new names. Specifically, any RBOC could establish a new affiliate (which did not meet the requirement of §251(h)(1)(A) of the 1996 Federal Act of providing local exchange service as of the date of its enactment), transfer part or all of its assets to the new affiliate, and continue its monopoly over the local exchange market in a particular area without complying with the ILEC requirements. OCC notes that the FCC has previously foreclosed this possibility by not permitting BOCs to transfer local exchange and exchange facilities and capabilities to another affiliate in order to evade regulatory requirements. Therefore, OCC recommends the Department interpret §251(h)(1) of the 1996 Federal Act consistent with the FCC's guidance. OCC Brief, pp. 8-18; OCC Reply Brief, pp. 15 and 16.

OCC further claims that the Public Act establishes a statutory framework and procedures that decrease the level of regulation accorded to increasingly competitive services. OCC states that the only reason SNET eschews the established reclassification procedure is that adhering to such procedures is too heavy a burden and the outcome is too uncertain. OCC argues that neither SNET's convenience nor its desire for a pre-ordained outcome is adequate justification for evading important proceedings and procedures established by the Department and by the Act. OCC maintains that an examination of SNET's market power suggests that the local exchange service market in Connecticut is not competitive and is not ready for the less rigorous regulatory treatment that accompanies a competitive classification.

Moreover, OCC asserts that the Company possesses virtually 100% of the market coupled with the enormous power of incumbency. OCC, while acknowledging the number of certified CLECs, contends that the presence of these service providers will not ensure proper price protection to retail end users. OCC maintains that no amount of economic theory can alter the fundamental fact that the Company retains monopoly power in the provision of local exchange service in Connecticut, particularly for residential and small business consumers. OCC also disagrees with the Company that Connecticut's present retail markets are as close to perfectly contestable as conceivable and SAI would have little or no market power. According to OCC, the fatal weakness of the theory of contestable markets is that it does not apply in the real world. OCC Brief, pp. 22-26.

3. Customer Marketing

In response to the Company's proposed information campaign, OCC believes that there is merit to a proposal to disseminate information to the ratepayers of Connecticut concerning the ramifications of the implementation of the Public Act as well as the 1996 Federal Act. OCC does not believe, however, that it is practical to fund and staff an "answer center" or "information booth" structure since either would be cumbersome and probably lead to improvident sales opportunities. OCC also notes that there is no interest on the part of the Company's competitors to participate in a program in which independent salespeople would be answering customer questions on behalf of all service providers.

As an alternative to the Company's proposal, OCC suggests that an information package be drafted by a committee of the Department, OCC, and other parties to this proceeding and made available to affected customers. OCC states that while there is plenty of information being disseminated in the media, state regulatory bodies could best orchestrate an impartial and informative brochure or letter with basic "how to" customer information. OCC suggests that developed materials be disseminated as information provided by the Office of Consumer Counsel pursuant to an order from the Department. OCC Brief, pp. 28 and 29.

4 Affiliate Transactions

OCC argues that affiliate transactions contemplated by the Company's proposal place customers at risk because the inadequacy or inapplicability of affiliate transaction rules will allow the Telco to discriminate in favor of SAI. OCC disagrees with the Company that the proposed transfer of assets to SAI are not a "transaction" for purposes of its Cost Allocation Manual. According to OCC, in those cases where SAI will compensate the Telco for assets, compensation is set at "net book value" instead of market value. OCC is of the view that other market participants must obtain these same assets at market value if they are to challenge SAI's market position.

OCC also contends that a single affiliate transaction, the transfer of the Telco's customer base, would provide SAI with one of the greatest advantages it would receive under the proposal,. OCC contends that by allowing SAI to receive the entire customer base at no cost, the Department would severely disadvantage other participants who would have to incur significant costs to make inroads into the local market. According to OCC, under this scenario, competition would be impeded and consumer protection would be withheld.

Lastly, OCC claims that the purpose of examining the affiliate transactions is to ensure that there is no cross-subsidization between services performed by the company for any of the competitive affiliates. Tr. 4/3/97, p. 605. OCC argues that SNET's proposal would result in exactly that type of cross-subsidization. OCC asserts that competition would be impeded because SAI would receive through its affiliation with the Telco a lower cost of capital than if it had to obtain funding on its own, as other market participants will. OCC Brief, pp. 28-31.

C. AT&T COMMUNICATIONS OF NEW ENGLAND (AT&T)

1. 1996 Federal Act

AT&T contends that the Company's proposal is patently illegal and a violation of §§251 and 252 of the 1996 Federal Act and inconsistent with the reasoning and intent of §272 of that act. AT&T states that the Company is an ILEC as defined by the 1996 Federal Act and is subject, regardless of corporate structure, to all the obligations of an ILEC. AT&T claims that the Company as currently structured and primarily through the proposed SAI and Telco entities clearly meets the requirements set forth in §251(h)(1)(A) and (B) of the 1996 Federal Act and will retain the obligations of an ILEC under the 1996 Federal Act. AT&T Brief, p. 5.

AT&T argues that §251(h)(2) of the 1996 Federal Act makes explicit the intention that responsibilities of an ILEC never go away. AT&T asserts that while in the future the Company may be composed of many subsidiaries and may transfer functions, assets and employees between or among these subsidiaries, there must always be an ILEC to fulfill all of the ILEC responsibilities of the 1996 Federal Act. According to AT&T, until another carrier has been designated by the FCC as having replaced the Telco as the ILEC, then the Telco retains the responsibilities of an ILEC. AT&T contends that there is no other carrier capable of fulfilling these functions within SNET's territory, nor has the FCC named another carrier. The Company is therefore required to fulfill all of the ILEC responsibilities.

AT&T also argues that the 1996 Federal Act is explicit as to the circumstances under which an ILEC may be exempted from specified requirements. AT&T maintains that the 1996 Federal Act does not provide for the restructuring of the corporate entity in the manner proposed by the Company or it would exempt the Company from its ILEC responsibilities. AT&T also maintains that the Company is not (as suggested by SNET) divesting itself of its retail or wholesale operations; rather, it is providing retail services to end users and wholesale services to CLECs.

Additionally, AT&T contends that the FCC has specifically addressed the separate affiliate issue as it relates to the BOCs and this reasoning is as true for the Company as it is for an RBOC. In AT&T's view, it is apparent from §272 of the 1996

Federal Act that local exchange carriers may not circumvent their resale obligations by restructuring themselves into different arm's-length subsidiaries. According to AT&T, § 272 of the 1996 Federal Act requires RBOCs in certain circumstances, such as the provision of out-of-region interstate services, to establish arm's-length subsidiaries that are separate from any "operating entity" subject to the resale requirements in §251(c) of the 1996 Federal Act. AT&T notes that although §272 of the 1996 Federal Act specifically permits and requires RBOCs to establish arm's-length subsidiaries to provide certain services, it also requires that a separate "operating entity" be maintained to fulfill the carrier's resale obligation.

AT&T maintains that the intent of the 1996 Federal Act is to ensure that the RBOCs could not accomplish through a separate subsidiary what they were prohibited from doing as an ILEC (i.e., combining monopoly operations with competitive long distance service and leveraging their bottleneck). While noting that §272 of the 1996 Federal Act does not directly apply to the Company because it is not an RBOC, AT&T maintains that the Company must not be permitted to leverage its ownership of bottleneck facilities and should be held to its resale obligation, as are RBOCs, irrespective of whether it creates separate wholesale and retail subsidiaries.

AT&T concludes that restructuring in and of itself does not relieve the Company of or allow it to otherwise narrow its ILEC responsibilities under the 1996 Federal Act. AT&T suggests that if the Company's proposed restructure could produce such a result, then all ILECs could similarly restructure themselves to circumvent their ILEC responsibilities under the 1996 Federal Act. AT&T claims that the Company's interpretation of the 1996 Federal Act would render the concept of an ILEC meaningless. AT&T Brief, pp. 6-11.

2. Retail and Wholesale Service Pricing

Additionally, AT&T argues that nowhere does the 1996 Federal Act permit ILECs to "freeze" their retail offerings at a given point in time, so that the ILEC no longer has to offer its retail services for resale. AT&T states that ILEC resale obligations are clear with respect to retail services, including the requirement that they make available any retail telecommunications service that it provides to end users for resale at wholesale discounts. AT&T states that the Company is not divesting itself of its retail operations but is merely establishing separate wholesale and retail subsidiaries. AT&T argues that the Company is continuing to provide retail services, albeit through a subsidiary, and under the 1996 Federal Act must make such telecommunications services available for resale.

AT&T also contends that the Company's proposal to price new wholesale services at cost plus contribution rather than at a wholesale discount, is contrary to the pro competitive resale requirements of both the 1996 Federal Act and the FCC Order. AT&T argues that all of SAI's retail services must be offered for resale at the retail rate, minus avoided costs. According to AT&T, the Company, through the Telco or otherwise, must offer its retail services for resale at a wholesale discount irrespective of the fact that it offers those retail services through a separate arm's-length subsidiary.

AT&T suggests that if SAI were excused from its resale obligations, SAI could begin to change the prices, terms and conditions of its retail services, filing them as new services not available for resale. In AT&T's view, by use of such a loophole, SAI could create a whole new class of retail services and price these services lower than those that would be available for resale at a wholesale discount. AT&T maintains that this is in violation of the resale obligations of the federal law, has dangerous implications on the competitive viability of current CLECs and the potential to chill any new entry by CLECs.

AT&T states that ILEC obligations to resell, unbundle and interconnect are the tri-part cornerstone of Congress' effort to pry open the local marketplace to competition. According to AT&T, the fact that the Telco will offer new wholesale services at TSLRIC plus contribution does not satisfy the requirements of the federal law. AT&T also states that the 1996 Federal Act explicitly states that any telecommunications service offered at retail must be made available at a wholesale discount. AT&T argues that offering new wholesale services at TSLRIC plus contribution simply does not fulfill the Company's resale obligation. AT&T Brief, pp. 11-15; AT&T Reply Brief, pp. 6-13.

3. Service Reclassification

AT&T further argues that Public Act 94-83 prescribes procedures and requirements to reclassify a service as a competitive service. AT&T contends that the Company's proposal does not meet these procedures or requirements and would allow it to avoid the requirements of the Department's price cap regime. Accordingly, AT&T asserts that the Company's proposal must be rejected.

AT&T argues that as a matter of law, the Department lacks authority to reclassify SAI services as competitive in the manner proposed by the Company. According to AT&T, the Act classified only a very few of the Company's services as competitive, while the majority of its regulated services remain in the non-competitive category. AT&T states that the Act also established procedures whereby the Company could petition the Department to change the classification of a service. The Company's restructuring plan ignores these requirements and assumes that all retail services provided by SAI would be competitive. AT&T maintains that the Company should be required to fully comply with the requirements of the Act and the Department's reclassification procedures before any of its services can be reclassified, irrespective of whether they are provided by the Telco, SAI or any other subsidiary.

Additionally, AT&T disagrees with the Company's claim that once SAI's application for a CPCN is approved all services provided by SAI as a CLEC "will be deemed 'competitive' telecommunications services." AT&T argues that the issue before the Department is not whether services provided by a CLEC are competitive by virtue of being provided by the CLEC. Rather, the issue is whether, under the Act, the Department must: (1) follow the procedures established for determining the classification (i.e., non-competitive, emerging-competitive, competitive) of each of the individual services the Company proposes to transfer to SAI; (2) determine in accordance with this procedure that each of the services to be transferred is competitive; and (3) do so before it approves the transfer of any service it finds to be competitive to SAI, to the extent it approves SAI's application as a CLEC.

Regarding the Company's proposal that the Department reclassify its services as competitive based upon the criteria contained in Conn. Gen. Stat. §16-247(f)(d), AT&T contends that the Company's presentation is inadequate. According to AT&T, a mass reclassification of the Company's retail services, under any circumstances, is clearly inappropriate. AT&T states that the express language of the statute, as well as the legislative history and intent of the Act, envisioned a service-by-service reclassification procedure wherein the Department would consider eight criteria before deciding whether to reclassify a service. AT&T also states that the instant docket was not established to reclassify services nor did the parties have an opportunity to evaluate and respond to the Company's alleged proffer of proof. AT&T suggests that if the Company wishes to reclassify its services it should do so in the context of a docket where such issue is expressly presented.

AT&T states that in addition to circumventing its obligations under the Act, the Company is seeking to remove itself from price cap regulation as established by the Department in its March 13, 1996 Decision in Docket No. 95-03-01. AT&T claims that under the Company's reorganization proposal, retail prices will be no longer subject to any price ceiling, even if the services were not yet competitive and the ratepayers would receive no protection whatsoever. According to AT&T, the Company's proposal to escape obligations imposed on it by the alternative regulation plan violates Public Act 94-83 and the Decision in Docket No. 95-03-01. AT&T therefore suggests that the Company's proposal be rejected. AT&T Brief, pp. 16-22; AT&T Reply Brief, pp. 14 and 15.

4. Arbitrated Awards

AT&T also argues that the Company's proposal to resell only those retail services that exist in its retail tariff as of the effective date of any allowed restructure and to price all new wholesale offerings at cost plus contribution violates the AT&T/SNET arbitration award and must be rejected. AT&T maintains that as part of the Department-approved Arbitration Award between AT&T and SNET in Docket No. 96-08-08, Application of AT&T Communications of New England, Inc. for Arbitration with the Southern New England Telephone Company Under the Telecommunications Act of 1996, the parties agreed that:

> SNET shall tariff and make available to AT&T, at wholesale rates, all of SNET's retail telecommunications services on the same terms and conditions contained in the retail tariffs for those services, except as otherwise specifically set forth in this Agreement. [11]

AT&T claims that at no time during these negotiations did SNET indicate its

[11] Docket No. 96-08-08, Decision, dated December 4, 1996, p. 12.

intention to limit the availability of retail services in the manner or time frame as proposed in the instant proceeding. AT&T contends that the Company should not be permitted to change the agreement the Company entered into before it filed its January 24, 1997, restructuring proposal. AT&T asserts that the Department has established that the arbitration awards should take precedence over any generically established rates. Therefore, the Company should not be permitted to change rates specifically awarded as part of the arbitrations, especially those rates which were negotiated and agreed to for a specified period of time. AT&T Brief, pp. 22-25

5. Market Contestability

AT&T states that the level of deregulation sought by the Company is not commensurate with the level of competition present in the local exchange service marketplace and is unnecessary in light of the current regulatory framework in Connecticut. AT&T claims that the Company's proposed restructuring will unleash the incentives and opportunities dominant monopoly providers of services have at their disposal to discriminate against potential rivals. According to AT&T, these incentives and opportunities would present significant hazards to the continued development and growth of local exchange competition in Connecticut.

AT&T also disagrees with the Company's claim that the local exchange market in Connecticut is contestable because the 1996 Federal Act has put in place provisions designed to remove barriers to competitive entry. AT&T states that the Company's reliance on these provisions to demonstrate the contestability of the market allows the Company to ignore the fact that these are the same provisions it (the Company) admits it seeks to circumvent by its proposed restructure. Further, AT&T disagrees with the Company's claim that in order to determine contestability, the market to be analyzed is the totality of the local, intrastate and interstate toll markets. AT&T argues that the appropriate market is the local exchange marketplace and would not be contestable if: (1) the wholesale portion of the firm (Telco) finds subtle but effective ways to discriminate in favor of its retail subsidiary (SAI) and (2) new entrants must incur considerable sunk costs to enter the local market.

In AT&T's view, circumstances which prevent a market from being contestable are exactly those which exist in the present Connecticut local exchange service market. AT&T asserts that if SNET's proposal is approved, the Telco will have many opportunities to discriminate in favor of SAI. For example, the Telco and SAI possess an ability to share pre-existing billing and electronic ordering, provisioning, maintenance and repair arrangements, while new entrants will be required to develop, deploy and pay for such arrangements with the Telco. AT&T posits that the Telco could slow down or hinder the development of such interfaces with new entrants, while maintaining and strengthening the built-in advantage SAI enjoys by virtue of its pre-existing interfaces.

While SAI has reserved the right to negotiate and sign separate interconnection agreements with the Telco, AT&T claims that no new entrant can expect to negotiate term and volume discount arrangements as attractive as those to be made available by the Telco to SAI. AT&T asserts that no new CLEC could hope to penetrate the local marketplace because SAI will be able to offer lower prices than its competitors because of SAI's pre-existing relationships with the incumbent.

Finally, AT&T maintains that the Company's attempt to circumvent the Act's specific imputation standard presents it with another opportunity to discriminate against CLECs by placing them in a price squeeze hindering local market entry. AT&T asserts that the Company wishes to eviscerate the imputation standard by agreeing to an aggregate imputation standard. According to AT&T, an aggregate imputation standard allows the Company to demonstrate that over a broad spectrum of services its prices in total or in aggregate are greater than the corresponding wholesale prices charged to competitors. AT&T states that this would allow the Company to maintain high prices for some services (e.g., toll), while placing its competitors in a price squeeze for local services. AT&T contends that an effective service-by-service imputation standard must be in place.

Additionally, AT&T argues that the theory of contestable markets assumes entrants do not have sunk costs. AT&T states that this is not the case in the Connecticut local exchange market because resellers and facilities-based carriers have sunk costs of entry, although the level of sunk costs for resellers may be lower. AT&T cites as an example the marketing costs of getting customers to switch their carriers. AT&T also claims that new entrants must expend substantial time and costs in developing billing systems and electronic interfaces with the Company for ordering, provisioning, maintenance and repair, etc., expenses which SAI will not experience. AT&T also claims that the development and deployment of these systems have been a major hurdle for it to enter the local market on a ubiquitous basis and in conformance with the quality of service expected by today's customers.

Furthermore, AT&T contends that only when sufficient alternatives exist to the Company's resale services and unbundled network elements, will competitive local exchange carriers be freed from the Company's monopoly grip and be able to shop elsewhere for these services. AT&T states that only when facilities-based competition truly develops will CLECs have the ability to purchase resale or unbundled network elements from other sources. Until then, the Company's reorganization proposal is seriously premature, because discriminatory behavior by it or its subsidiaries, or failure to enforce an effective imputation standard will hinder competition in the local market.

AT&T disagrees with the Company's suggestion that the relevant market that should be examined in order to determine whether the level of competition justifies the extensive deregulation sought by the Company is the combined local, intraLATA toll and interstate market. AT&T asserts that examining these very distinct markets in aggregate will serve to obfuscate the level of competition present in each especially the local marketplace. Noting that the Company has admitted to retaining over 99% of all local customers, AT&T states that it is ridiculous to argue that an ILEC who owns the local bottleneck network and maintains more than a 99% market share should be granted the type of price deregulation for its local services sought by the Company. AT&T also states that the Company has been providing intraLATA toll service as the incumbent LEC for over 100 years while other carriers were not permitted into this market until 1988, and could not effectively compete until intraLATA presubscription was fully deployed at the end of 1996. AT&T maintains that the Company has an enormous advantage in the intraLATA toll market place due to its ability to leverage its position as the local service provider for more than 99% of Connecticut's customers. SNET, by virtue of reclassifying its intraLATA toll service as a competitive service, has all the pricing flexibility it needs to compete in this market.

AT&T contends that SNET has been very successful in the interstate toll marketplace gaining more than 30% of the market share. SNET is not required to resell its interstate toll services at a wholesale discount and, therefore, is not disadvantaged in this market by its resale obligation imposed by federal law. AT&T concludes that the Company's resale obligation has not resulted in any appreciable erosion of its monopoly hold over the local market. Additionally, the Company's resale obligation does not materially affect the dynamics of the intraLATA market where its largest competitors do not resell its services or the interstate market where it is very successful and is not obligated to resell its services at a wholesale discount. AT&T Brief, pp. 26-34.

6. ILEC Obligations

AT&T argues that the reason the 1996 Federal Act and FCC place resale, unbundling and interconnection obligations on an ILEC is to open the monopoly hold they have on the local exchange market. AT&T disagrees with the Company's contention that the 1996 Federal Act and FCC's implementing orders place onerous asymmetric regulation on an ILEC such that it will be unable to compete against CLECs in terms of price, product innovation or service. According to AT&T, the Company continues to retain its competitive advantage by virtue of the fact that it has the vast majority of local customers in the state, owns the existing bottleneck local network, is not burdened with the enormous costs of initial local market entry as are CLECs, and has been extremely successful in the long distance market. AT&T states that the Company's claim that it is at a competitive disadvantage to new entrants trying to break into the local market strains credulity.

AT&T also disagrees with the Company's argument that the Telco's obligation to offer for resale new innovative service packages prevents it from effectively competing with new entrants. AT&T claims that the Company's argument is flawed in two fundamental respects. First, the historical development of competition in the interstate marketplace has shown that resale of long distance services has not hindered innovation and competition. Citing its own experience in the interstate market, AT&T states that it has not been precluded from offering innovative, long distance services, and notes that the long distance marketplace is now characterized by an abundance of innovative competitive offers, (e.g., SNET's All Distance, MCI Friends and Family, and Sprint 10¢ A Minute). Additionally, AT&T states that of the six services which the Company claims will be included in service packages that will be increasingly prevalent in a competitive marketplace (i.e., local service, interstate and intrastate toll, video, wireless and on line services), only two must be made available for resale at wholesale discounts under the 1996 Federal Act and FCC Order whether included in a package or not, (i.e., local and intrastate toll services). AT&T states that the other four services are not required to be made available for resale at wholesale discounts. AT&T notes that the Company's largest CLEC competitors provide intrastate toll services over their own networks and it is unlikely that they would seek to resell these services from the Telco.

AT&T also disagrees with the Company's claims that it (the Company) is at a competitive disadvantage when reselling promotional offerings of greater than 90 days. AT&T asserts that the Company ignores the fact that for promotions of 90 days or less, it has a competitive advantage over CLECs because ILECs are not required to resell such promotions at a wholesale discount. According to AT&T, the FCC has struck a balance between the benefits of short term promotions and the potential for abuse of long term promotions by limiting the ILEC's resale obligation to promotions exceeding 90 days. AT&T argues that the Company should not be permitted to circumvent its resale requirements with respect to such promotions by creating an arm's-length subsidiary.

Regarding the Company's claim that its ability to differentiate its retail services from those offered by CLECs is limited because it is required by law to resell those same retail services , AT&T states that the Company ignores the fact that it is an ILEC who owns the bottleneck and local network. AT&T claims that this is precisely the reason new entrants must purchase wholesale services and unbundled elements from an ILEC at a discount in order to enter the local market on a widespread basis. AT&T maintains that the requirement that the service an ILEC provides to CLECs must be at parity to the service it provides to itself and to its customers is necessary because an ILEC could hinder local market entry if it were permitted to offer wholesale services and unbundled network elements to new entrants at less than parity. AT&T contends that the inability to purchase services from an ILEC at parity with the quality offered in the ILEC's retail services tilts the competitive playing field to the ILECs.

AT&T asserts that the Company's reorganization proposal will do nothing to remedy the Company's perceived disadvantage in the market. AT&T states that since SAI will resell the Telco's services and will be subject to the same general prices, terms and conditions as any other CLEC, SAI's retail services will always be at quality parity with any other CLEC who purchases services from the Telco. AT&T further states that even if SAI paid a premium to the Telco for better service quality for certain services, any other CLEC could presumably pay the same premium and purchase the same quality of service. AT&T concludes that the Company's argument that its service parity obligations vis-à-vis its retail and CLEC customers places it at a competitive disadvantage and, therefore, justifies its proposed reorganization is without merit. AT&T Brief, pp. 34-45; AT&T Reply Brief, pp. 21 and 22.

7. Level of Regulation

Additionally, AT&T disagrees with the Company's claim that its reorganization plan will leave SAI in exactly the same situation as any other CLEC. AT&T contends that SAI would retain significant advantages over new entrants. For example, unlike any other new entrant, SAI will come into existence with the transfer of all of the telephone company's current residential and business local customers, making it the largest CLEC in Connecticut. Furthermore, AT&T contends that SAI will inherit an established and recognized brand name, operational linkages with its wholesale provider (Telco) and the Directory Publishing units, and an incumbent corporate parent that also owns the monopoly local network and numerous related enterprises which SAI is likely to employ in developing bundled service offerings to its end user customers. AT&T argues that these advantages as the successor of the Company are a significant value that SAI's competitors do not have, and set SAI apart from and in a more favored position than its competitors. Therefore, AT&T concludes that SAI should not be regulated as a CLEC. AT&T Brief, pp. 45-52.

8. Customer Marketing

Regarding the Company's customer notification proposal, AT&T claims that it is unfairly discriminatory. AT&T states that it would be difficult to design a center that is completely competitively neutral, especially when the Company proposes to fund the center. AT&T concludes that the Company's proposal to fund a competitively neutral information center should be rejected. According to AT&T, the proposed information center would provide little, if any benefit, to the average consumer and serve only to confuse most customers. AT&T contends that the only carrier who would benefit from this confusion would be the incumbent. AT&T Brief, pp. 53-55.

9. Company Regulatory Structure

Lastly, AT&T argues that despite the Company's assertions, transferring retail services to SAI, where it will avoid almost all state regulation, is not necessary to allow SNET to compete effectively in the local market. AT&T states that Connecticut anticipated, and planned for, the development of local competition with the passage of Public Act 94-83. AT&T maintains that under the authority of the Act, SNET sought and was allowed a form of alternative regulation. The regulatory structure now in place in Connecticut was carefully designed to facilitate and encourage the development of competition, including the Company as one of the competitors. AT&T asserts that the Company should not now be allowed to restructure and escape regulation over its retail services entirely.

AT&T claims that in further pursuit of the legislative goal to match the level of regulation to the level of competition, the Act encouraged the Department to implement an alternate form of regulation. The Company proposed, and the Department accepted, a plan that provides separate pricing mechanisms for noncompetitive, emerging competitive and competitive services. According to AT&T, the alternative regulation plan gives the Company increasingly greater pricing flexibility as the level of competition increases.

AT&T asserts that it is critical to recognize that there still is not significant local service competition in Connecticut. AT&T comments that SNET has not sought to reclassify local service as other than a noncompetitive service. AT&T also asserts that the proposed reorganization plan is an attempt to avoid the alternative regulation structure entirely with respect to its retail services. AT&T states that the Public Act and the alternative regulation plan approved by the Department in Docket No. 95-03-01, recognizes that a continuing, but decreasing, level of regulation is necessary and appropriate during the transition from a monopoly environment to a truly competitive marketplace. AT&T argues that SNET has not presented any evidence in this docket to change the conclusion reached in Docket No. 95-03-01 that the decreasing level of regulation provided by the alternate regulation plan is the appropriate way to deal with this period of transition. AT&T Brief, 55-59.

D. MCI TELECOMMUNICATIONS CORPORATION (MCI)

1. Reorganization Proposal

MCI states that when viewed in the context of the Connecticut Telecommunications Task Force's work, the new regulatory compact established by the Connecticut Legislature under Public Act 94-83 and the Department's efforts over the past three years to implement the Act, the Company's proposal squarely conflicts with the state telecommunications law and policy as carried out by the Department over the past three years. MCI claims that SNET has ignored the Department's admonition at the outset of this proceeding that "SNET's affiliate strategies, structures and standards conform with the prevailing rules and regulations governing telecommunications providers"[12] and has recommended a proposal that far exceeds the scope of the instant docket.

MCI argues that the Company's proposal fails to comply with the requirements of the Act applicable to the reclassification of telecommunications services. MCI also argues that since SNET has not complied with the service reclassification process and admitted that its proposal is not a request for service reclassifications in accordance with §16-247f of the Conn. Gen. Stat. the Department is without any statutory authority to reclassify SNET's retail services. MCI maintains that SNET can only transfer or assign noncompetitive services to SAI and that SAI cannot acquire as successor to SNET any service classifications other than those held by SNET at the time of such transfer or assignment.

MCI asserts that SNET's proposed plan violates the Decision in Docket No. 95-03-01 that approved an alternative form of regulation for SNET, as well as Conn. Gen. Stat. §16-247k, which authorizes and limits the alternative form of regulation available for adoption by the Department. According to MCI, the alternative form of regulation previously adopted by the Department expressly made the Company's retail services subject to the service reclassification requirements of Conn. Gen. Stat. §16-247f, for the term of the approved plan. MCI contends that the Company's proposal violates service reclassification requirements in that the effect of approval of the proposed plan constitutes a reclassification of all of SNET's telecommunications services to the competitive category without regard to the substantive or procedural requirements of Conn. Gen. Stat. §16-247f or the Department's Decision in Docket No. 95-03-01. MCI

12 Statement of Scope of Proceeding, p. 2.

concludes that approval of the proposed plan would exceed the Department's statutory authority and conflict with the Decision in Docket No. 95-03-01. MCI argues that the Company should not be allowed to circumvent Conn. Gen. Stat. §16-247f through the artifice of a corporate restructuring.

MCI further asserts that under the above circumstances, the Company is effectively barred from implementing its proposed restructuring plan due to its corporate decision to operate under an alternative form of regulation. According to MCI, all of the pricing provisions of the price cap plan presume the offering of retail services by the Company during the entire term of the plan. MCI states that these provisions further incorporate the service reclassification requirements of Conn. Gen. Stat. Section 16-247f, and the Company's reorganization proposal is in direct conflict with these requirements.

Additionally, MCI argues that the Company's proposal conflicts with the underlying basis for development of all existing retail rates. MCI contends that the Company's proposal to split up its telecommunications services and its existing corporate functions destroys the underlying basis for the "going in" rates approved by the Department when adopting its alternative regulation plan and makes the review and monitoring of the Company's earnings virtually impossible. MCI is of the view that functions and costs that were covered by the alternative form of regulation are now proposed to be split up into at least three affiliates: the holding company, the Telco and SAI. MCI states that the Company's proposal conflicts with the existing alternative form of regulation and cannot be approved. MCI also states that this fatal flaw transcends the form of regulation that must apply to SAI because it goes to the very inability of the Company to restructure at the onset of an alternative form of regulation. MCI maintains that such a restructuring squarely conflicts with the earnings monitoring portion of the current form of regulation, as mandated by Conn. Gen. Stat., §16-247k.

MCI contends that approval of the Company proposal will be contrary to the overall objectives of the Act relative to the requirement that the State "utilize forms of regulation commensurate with the level of competition in the relevant telecommunications service market...." This goal will be frustrated if the Company can avoid the service reclassification provisions of Conn. Gen. Stat., §16-247f merely by restructuring.

MCI states that the Company's restructuring proposal affords no basis for modifying the form of regulation now in place. MCI also states that this is not a case where the Department may modify the current plan for an alternative form of regulation in accordance with §16-247k(e) of the Conn. Gen. Stat. MCI argues that no modifications can be deemed necessary due to previously unforeseen circumstances. According to MCI, the fundamental inconsistency between the alternative form of regulation under which SNET now operates and its current restructuring proposal does not constitute a "previously unforeseen" circumstance. MCI further states that neither the Company nor the Department have ever indicated that the present case involves the issue of modification of the alternative plan of regulation approved in Docket No. 95-03-01. MCI Brief, pp., 11-17; MCI Reply Brief, p. 9-13.

2. 1996 Federal Act

MCI also argues that the Company's reorganization proposal violates the letter and spirit of the 1996 Federal Act. MCI asserts that the Company is bound by the ILEC obligations contained in the 1996 Federal Act. If the Department approves the proposed plan as filed, MCI contends that SAI must be regulated as an ILEC until it can prove that effective and sustainable competition exists in the local market. MCI also asserts that SAI must be considered a "successor or assign" of the Company and accordingly regulated as an ILEC in order to stimulate such competition in Connecticut.

MCI disagrees with the Company that upon the effective date of the restructuring SAI would not be a successor or assign of the Company and should not be treated as an ILEC. MCI contends that SAI, as proposed, is a successor or assign of the Company and must be considered an ILEC pursuant to §251(h) of the 1996 Federal Act. MCI states that any other interpretation of the statute would result in an essential failure of the goals and obligations of the 1996 Federal Act and the Company should not be allowed to circumvent its obligations under the FTA by restructuring.

MCI cites to the 1996 Federal Act at §251(c)(4)(a) which requires ILECs to "offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers;" and Section 252(d)(3) that an ILEC's wholesale rates be set on the basis of retail rates charged to subscribers for the telecommunications service requested excluding the portion of that rate that will be avoided through wholesale provisioning. Based on these sections, MCI argues that retail and wholesale prices are linked, thereby preventing price squeezes and encouraging competition. MCI contends that through its proposed corporate restructuring the Company intends to break the linkage between retail and wholesale pricing and essentially evade the resale obligation mandated for ILECs under the 1996 Federal Act. MCI claims that upon approval SAI will be able to offer discounted packages and products to subscribers but would have no corresponding obligation to resell at a discount to competitors, while the Telco would not be obligated to resell the package because it would be provided by SAI. MCI asserts that the Company should not be able to avoid its obligations under the 1996 Federal Act merely by restructuring.

Additionally, MCI asserts that the Company's proposal to break the linkage between wholesale and retail rates violates existing arbitration agreements. MCI contends that if the proposed restructuring is approved and the Company is allowed to sever the link between retail and wholesale rates as of January 1, 1998, the wholesale discount that is contained in MCI's arbitration award would no longer be applicable and the Company's resale obligation would cease to exist. MCI argues that the Company cannot be permitted to avoid its resale obligations under the 1996 Federal Act, regardless of whether the obligations are contained in agreements resulting from arbitration or generic proceedings. MCI Brief, pp. 17-21.

E. New England Cable Television Association, Inc. (NECTA)

1. Reorganization Proposal

NECTA opposes the Company's proposed reorganization plan, arguing that it violates the provisions of the 1996 Federal Act and Public Act 94-83 which were designed to protect against use of ILEC monopoly power over local exchange telephone markets and control over bottleneck facilities to hinder competition. NECTA recommends that the Department not accept the Company's attempt to evade these statutes. NECTA also argues that the Company's reorganization proposal violates the pro-competitive policies underlying the state and federal laws. According to NECTA, SNET's noncompliance with both the statutory provisions regulating incumbent LECs and the procedural provisions established in each statute for obtaining relief from the ILEC regulation undercut any claim that the Company's reorganization plan is consistent with the policies underlying the 1996 Federal Act and Public Act 94-83. NECTA also argues that the reorganization plan imposes significant potential harm and cost on consumers, CLEC competitors, and the Department and other public agencies, with few, if any, corresponding benefits to the public. NECTA Brief, pp. 3 and 4.

2. 1996 Federal Act

NECTA asserts that the Company's proposed reorganization plan violates the 1996 Federal Act. NECTA maintains that the Company is subject to the 1996 Federal Act §251(c)(4) obligations, which require the Company to resell all retail services offered to end user customers at a regulated avoided cost discount. NECTA contends that the Company cannot escape this or other ILEC obligations by means of a corporate reorganization. According to NECTA, the 1996 Federal Act defines an incumbent LEC to include any successor or assign, thereby barring ILECs from using a corporate reorganization among related entities to evade ILEC responsibilities. NECTA argues that one or both of these broad, corporate reorganization/transfer concepts must apply to SAI. NECTA also argues that the Company's proposed reorganization is the activity the successor or assigns language was intended to address: a paper transfer among related entities that shifts the ILEC's right to serve a near-ubiquitous customer base to an affiliate while eliminating obligations that protect competitors and the public from the exercise of monopoly power. NECTA asserts that the Department should not second guess Congress' decision to impose asymmetric regulatory burdens on incumbent LECs and other LECs based on relative degrees of market power and control over bottleneck facilities. NECTA Brief, pp. 5-9; NECTA Reply Brief, pp. 2-6.

3. Public Act 94-83

NECTA also contends that the Company's plan violates Public Act 94-83. According to NECTA, that alone provides a separate and independent legal basis for the Department to reject the Company's reorganization proposal. According to NECTA, the Connecticut Legislature deemed all of the Company's telecommunications services as noncompetitive except as otherwise enumerated in the statute. NECTA notes that the classifications for a service may be changed only pursuant to Conn. Gen. Stat. §16-247(f)(c), while under the Company's reorganization all retail local exchange services will automatically become competitive on the effective date of the reorganization.

NECTA claims that the Company has failed to comply with any of the reclassification procedures that it acknowledges are required by the Act. NECTA argues that the Act does not authorize the Company to obtain reclassification of noncompetitive services by merely transferring the service to an unregulated affiliate. NECTA states that to the contrary, Conn. Gen. Stat. §16-247(f) assigns the obligation to reclassify solely to the Department and does not provide for reclassification to occur upon exercise of a company's power to reorganize its affairs. Additionally, NECTA claims that the statute requires the Department to rule on the Company's compliance with the eight statutory factors, an impossibility based on the Company's admitted lack of a petition or materials to support compliance with these factors. NECTA maintains that the Company's failure to make the required filing to support reclassification under Conn. Gen. Stat. §16-247f requires rejection of the Company's reorganization proposal. NECTA Brief, pp. 9-12; NECTA Reply Brief, pp. 6 and 7.

4. Public Policy Concerns

NECTA also states that the Company's proposed reorganization represents poor public policy and should be rejected by the Department even if it is not found to be patently illegal. NECTA claims that the Company has failed to show that its proposal furthers the pro-competitive policies underlying the 1996 Federal Act and Public Act 94-83 or accords with the best interests of Connecticut ratepayers at this time. NECTA asserts that the proposed plan involves unnecessary costs, risk of harm and disadvantage to Connecticut consumers, CLECs and the Department. According to NECTA, the first and potentially most dangerous consequence of granting the Company's proposed reorganization would be to release a company with 95%-plus monopoly control over Connecticut local exchange markets and a 99%-plus share of the residential market from virtually all regulatory constraints. NECTA maintains that SNET possesses the ability to leverage its monopoly control over local exchange service to prevent competitors from offering a competitive bundle, thereby impeding competition.

NECTA also maintains that relieving the Company from its resale obligations eliminates the 1996 Telcom Act's fail-safe protection against anti-competitive behavior directed to facilities-based CLECs. According to NECTA, the Company's reorganization plan focuses on the use of resale and unbundling provisions in §251(c) of the 1996 Federal Act to open up an ILEC's network but ignores the resale obligation. NECTA acknowledges there are actions that a CLEC may take to deter or sanction anti-competitive behavior (i.e., bringing anti-trust complaints to the Department); however, NECTA suggests that the Department hesitate before removing this protection.

NECTA states that approval of the Company's reorganization plan will also require extensive regulatory oversight. NECTA claims that if the Company's plan is approved, procedural safeguards to protect the Company's competitors should be required to be implemented. These include holding the Company to an imputation standard, requiring periodic reports on costing of retail offerings, and requesting the Department to provide "close regulatory attention to anti-trust issues." NECTA Brief, p. 16. According to NECTA, these safeguards will provide limited benefits to an aggrieved competitor in a fast-changing competitive marketplace.

Additionally, NECTA argues that these safeguards involve high process costs (e.g., the need for CLECs, the Company, the Department and other public agencies to devote resources to fact-intensive regulatory investigations and proceedings). NECTA contends that the Department should not adopt the proposed reorganization plan and thereby avoid imposing these costs and burdens on the public, CLECs and the Department itself. NECTA recommends that the Department also follow the 1996 Federal Act by imposing regulatory restraints on the carriers with the greatest market power.

Further, NECTA argues that approval of the Company's plan will require renegotiation or rearbitration of interconnection agreements with other Connecticut LECs. NECTA states that this would cause uncertainty and delay for all CLECs in seeking to make or adjust their business plans for market entry. NECTA objects to this consequence of the Company's proposed plan. NECTA Brief, pp. 12-18.

5. Public Benefit

NECTA asserts that the proposed plan provides few, if any, benefits to Connecticut ratepayers. NECTA claims that granting regulatory relief to the Company at a time when it maintains a monopoly control over local markets will benefit its shareholders instead of the general public. NECTA also claims that lifting regulatory restraints currently imposed on the Company will not affect CLEC marketing efforts except to make their efforts less successful, drive up relevant costs, deter marginal entrants from joining the fray and, in general, delay the day Connecticut consumers finally will benefit from competition.

NECTA argues that benefits on the Telco side with reorganization are similarly insubstantial. NECTA states that it is not aware of any serious impediments that would prevent the Company from creating or expanding a new business unit and introducing new wholesale products today. NECTA maintains that relieving the Company of its resale obligation is not required because wholesale offerings need not be resold. NECTA concludes that the Company's proposed reorganization plan, if approved, would only provide minimal benefits to Connecticut ratepayers and therefore merits rejection by the Department.

Lastly, NECTA states that even if the Company's ability to compete is harmed by regulatory constraints, no action is appropriate until the Company's market losses are confirmed. In NECTA's view, the Department and the parties to this proceeding need to see whether and to what extent the Company's concerns will be borne out in the marketplace. NECTA claims that this approach fully accords with the interexchange market model. NECTA contends that granting relief now while competition has not yet taken hold is speculative and involves unnecessary risk of harm to the development of competitive telephone markets in Connecticut. NECTA argues that the Company is unlikely to suffer a major loss of market share in a short period. Noting that it has taken over a decade for AT&T's dominant share of the interLATA market to drop by one-third, NECTA suggests that the Department not act in haste and without data at this state in the development of competition. NECTA Brief, pp. 19-23; NECTA Reply Brief, pp. 7-10 .

VI. DEPARTMENT ANALYSIS

A. INTRODUCTION

This proceeding represents a continuation of the Department's effort to frame a telecommunications market in which all participants, incumbents and new providers, are afforded a fair opportunity to compete. Over the past three years, profound changes have occurred in state and federal telecommunications policy. As the Department acknowledged even at the beginning of its Public Act 94-83 implementation process, such changes would ultimately require an examination of the organizational constructs of SNET in the new competitive marketplace. The Department purposefully held this proceeding in abeyance until the competition and alternative regulation phases of the Public Act implementation neared completion, so as to permit full consideration of the changes resulting from that implementation and also from the 1996 Federal Act.

In simple terms, this proceeding has afforded SNET an opportunity to propose an organizational and operational structure it deems appropriate for the new telecommunications environment. The Department has reviewed the proposal to determine its impact on the development of broader competition in Connecticut's telecommunications market, its consistency with relevant state and federal laws and regulations, and its impact on the Connecticut public.

Before turning to the specifics of SNET's proposal, a brief historical review of the regulatory treatment of local exchange carrier organizations and operations will add to the understanding of this Decision. This proceeding represents a continuation of the Department's long term commitment to frame a competitive telecommunications market in which all participants, incumbents and challengers, are afforded sufficient opportunity to participate in the evolving information society of the next century. At the time the Department initially authorized this investigation in Docket No. 94-05-26, General Implementation of Public Act 94-83, it envisioned a proceeding where interested parties would be afforded opportunity to critique this Department's historical treatment of SNET's organizational and operational structures in the context of the multi provider market envisioned by Public Act 94-83 and to recommend any changes believed necessary to preserve consumer choice and promote competitive challenges in the market. The Department purposefully held this proceeding in abeyance until this time so as to permit it and the parties an opportunity to fully consider changes approved by the Department in conjunction with implementation of the Act and, subsequently, the 1996 Federal Act in the respective submissions.

This proceeding reflects the Department's need to examine potential consequences of adoption of any financial, structural and/or operational strategies presented by SNET as responses to material changes in state and federal telecommunications policy.[13] However, the interests of the Department in such strategies is limited to ensuring that such proposals do not impede the development and maintenance of broader market competition and that any increased discretionary authority afforded SNET comports with both state and federal statutes governing telecommunications policy. The Department expressed the opinion in Docket No. 94-05-26 that an objective examination of the organizational constructs and operational conduct of SNET in the new market place envisioned by Public Act 94-83 is critical to the development of competition in Connecticut. Accordingly, the Department set forth provisions in Docket No. 94-05-26 for such an inquiry early in the implementation planning process. Specifically, the Department foresaw needed changes in a number of regulatory policies and practices governing the industry in Connecticut to ensure that strategies, structures and standards employed by the subsidiary business units of SNET comport with the policies and practices adopted by the Department for a competitive market. To that end the Department docketed this proceeding and sought comment from interested parties.

B. REGULATORY CONTEXT

Over the past fifteen years, Congress, the FCC, the United States District Court for the District of Columbia, the Connecticut General Assembly and the Department have pursued policies and actions designed to broaden corporate participation in the segments of the telecommunications market. Collectively, they have sought via legislation, regulation, and adjudication to remove statutory and regulatory barriers that have historically limited the field of choice for the consumer. In so doing, state and federal representatives independently concluded that technological innovation by the telecommunications industry and thematic interdiction by the regulatory community are essential if financial and technological benefits enjoyed by the American public over the past 60 years are to be preserved for future generations.

With the initial introduction of a new competitive framework for the telecommunications industry in 1982, legislators and regulators selectively applied new rules, regulations and reporting responsibilities on LECs to ensure competitive parity among old and new members of the larger telecommunications community.[14] The LECs responded by introducing a series of organizational structures in which financial and operational agreements (generally referred to as affiliate relationships) were

---

[13] As the corporate parent of a certificated telecommunications provider in Connecticut, SNET is subject to, among other things, requirements previously imposed upon it by the Communications Act of 1934, as amended by the 1996 Federal Act, Public Act 94-83, and the First Report and Order issued by the Federal Communications Commission in CCDocket 96-149 "In the Matter of Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act of 1934, as amended".

[14] The first formal response by the FCC to the emergence of competition in the American telecommunications market was the Computer II rules issued in 1982 which established structural separation requirements for local exchange carriers that chose to engage in enhanced information services and to-be deregulated telecommunications products/services. The intent of these rules was to provide the LECs reasonable opportunity to engage in price competition while offering competitive entrants reasonable protections against cross-subsidization by the LEC.

employed as a means of restoring some of the lost linkage between various market segments and technology sectors served by the new subsidiaries of the LEC parent corporation. Issues regarding relationships between commonly-owned subsidiaries (generally referred to as affiliates) have generated debate for over a decade despite extraordinary efforts of both local exchange carrier management and regulators to assure the public of their prudence and propriety.

These facts suggest the presence of a broad strategic architecture dependent upon a set of affiliate business relationships intent on achieving goals that are otherwise denied to the LEC. The proposal made by SNET in this proceeding has expectedly regenerated debate over many of the issues that have marked this subject for over a decade. Yet the Proposal, if adopted, has the potential of reducing the scope and scale of affiliate transactions in contradiction to the general industry trend.

The concern expressed in this proceeding centers less on the number of affiliate relationships employed by the LEC and more on the nature of those relationships. It is a generally accepted principle of management that certain business relationships can be more important than others to the achievement of corporate goals and objectives. For regulated enterprises such as the Telco, it is essential to qualify that principle by noting that the corporate goals and objectives of the Telco must comport with those it is permitted to pursue by provisions of Public Act 94-83 and the 1996 Federal Act. It is the question of comportment and conformance with the prevailing statutory framework governing the telecommunications industry which the Department must address here.

In all of the implementation proceedings associated with Public Act 94-83, the Department has consistently sought to limit the scope and scale of regulatory participation in the state's telecommunications markets to that deemed necessary to protect the interests of the public and ensure fair opportunities for all market participants. In so doing, the Department has repeatedly affirmed its belief that the public is better served by broader competition than by broader regulation. That principle remains the cornerstone of the Department's telecommunications policy framework and is reaffirmed in this proceeding.

It has been suggested by some parties to this proceeding that regulation must be seen as a necessary restraint on the self-interested actions of the incumbent LEC and cannot be reduced without introducing significant risk of corporate abuse. The applicant in this proceeding, however, has argued that the presence of competitors and the increasing availability of product substitutions will serve to contain any excesses associated with its pursuit of business. The question of whether broad regulation is fundamental to market discipline is increasingly more a subject of academic debate and less a foundation principle of this Department's telecommunications policy. The concerted actions of the Connecticut General Assembly, the United States Congress and the Department have purposefully proscribed the Department's role in directing a competitive marketplace and that will not change with the outcome of this proceeding.

Over the years the regulatory community, including the Department at times, sought relative safety in the antitrust views of the early courts which concluded that monopoly's organizational structure was the key to both abuse by corporations of their privileged position and compliance with regulatory dictates. In the view of many jurists properly defined organizational structures could ensure responsible management action and full public accountability. Conversely, improperly defined organizational structures created the opportunity for misrepresentation and mismanagement, denying the public the full benefits of a free market. In consequence of that view, the identification and implementation of an "acceptable" operational structure which guaranteed active regulatory participation became a top priority in the minds of many in public service.

Critics of the post-divestiture telecommunications industry contend that operational structures which permit unconstrained growth and a broadened scope of business interest pose significant risk to the American public. However, it is important to note for purposes of this proceeding that the broad outline formula of the Modified Final Judgment left many questions of operational control, business definition, and entity relationships purposefully unanswered. Left with only general organizational instructions, management teams responsible for developing the proposed plans of reorganization followed similar paths and pursued common goals. The resulting organizational blueprints simply sought to (1) ensure compliance with the balkanized regulatory requirements of the signed agreement, (2) limit any customer inconvenience created by the events, and (3) minimize the financial and operational dislocations of the change. The planners had not been asked to concern themselves with the broad theoretical constructs of political power and economic containment subsequently raised in proceedings such as this and, accordingly, did not worry about them. Planners in the early 1980's were solely interested in satisfying the immediate needs of their shareowners, their customers and their regulators for a relatively efficient and effective delivery system.

In the decade since, however, regulatory agencies have been presented with questions regarding:

- the need for the complex network of interaffiliate transactions that support the current operational structure;
- the risk and/or benefit attendant to regulated customers by such relationships; and
- the extent of control exercised by management of the regulated units over their affiliate relationships.

This proceeding represents a notable departure from the previous affiliate interest investigation by the Department in Docket No. 89-09-02, DPUC Review of the Audit of the Affiliated Interests of Southern New England Telephone Company, and those undertaken by other state regulatory agencies which sought simply to understand the scope of affiliate transactions involving the Telco and ensuring those transactions were properly conducted, reported and accounted for by the Telco. This proceeding represents the first full-scale examination by the Department of the Telco's organizational structure under the terms and conditions outlined by Public Act 94-83 and the 1996 Federal Act.